



AUDITOR-GENERAL
SOUTH AFRICA

The Accounting Officer
Nkomazi local Municipality
Private bag X101
Malelane
1320

30 November 2018

Reference: 07464REG17/18

Dear Sir

Report of the Auditor-General on the financial statements and other legal and regulatory requirements of Nkomazi local municipality for the year ended 30 June 2018

1. The above-mentioned report of the Auditor-General is submitted herewith in terms of section 21(1) of the Public Audit Act of South Africa read in conjunction with section 188 of the Constitution of the Republic of South Africa section 121(3) of the Municipal Finance Management Act of South Africa (MFMA)
2. In terms of section 121(3) of the MFMA you are required to include the audit report in the local municipality's annual report to be tabled.
3. Until the annual report is tabled as required by section 127(2) of the MFMA the audit report is not a public document and should therefore be treated as confidential.
4. Prior to printing or copying the annual report which will include the audit report you are required to do the following:
 - Submit the final printer's proof of the annual report to the relevant senior manager of the Auditor-General of South Africa for verification of the audit-related references in the audit report and for confirmation that the financial statements and other information are those documents that have been read and audited. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.
 - The signature *Auditor-General* in the handwriting of the auditor authorised to sign the audit report at the end of the hard copy of the audit report should be scanned in when preparing to print the report. This signature, as well as the place and date of signing and the Auditor-General of South Africa's logo, should appear at the end of the report, as in the hard copy that is provided to you. The official logo will be made available to you in electronic format.
5. Please notify the undersigned Senior Manager well in advance of the date on which the annual report containing this audit report will be tabled.
6. Your cooperation to ensure that all these requirements are met would be much appreciated.

Auditing to build public confidence

Kindly acknowledge receipt of this letter.

Yours sincerely

Signed



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Thandi Boshoga
Senior Manager: Mpumalanga

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Report of the auditor-general to the Mpumalanga Provincial Legislature and the council on the Nkomazi Local Municipality

Report on the audit of the financial statements

Opinion

1. I have audited the financial statements of the Nkomazi Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2018, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Nkomazi Local Municipality as at 30 June 2018, and its financial performance and cash flows for the year then ended in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2017 (Act No. 3 of 2017) (Dora).

Basis for opinion

3. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of this auditor's report.
4. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Emphasis of matters

6. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

7. As disclosed in note 48 to the financial statements, the corresponding figures for 30 June 2017 were restated as a result of an error and reclassification in the financial statements of the municipality at, and for the year ended, 30 June 2018.

Material impairments – trade debtors

8. As disclosed in notes 11 and 13 to the financial statements, the receivables balance was significantly impaired. The total impairment of receivables from non-exchange transactions and consumer debtors amounted to R73 152 956 (2016-17: R138 153 935), which represented 82% (2016-17: 90%) of the total consumer debtors. The contribution to the provision for debt impairment was R6 669 036 (2016-17: R61 979 316).

Material losses – electricity

9. As disclosed in note 56 to the financial statements, material electricity losses of R6 041 606 (2016-17: R10 815 696) were incurred, which represented 12% (2016-17: 23%) of the total electricity purchased.

Unauthorised, irregular, and fruitless and wasteful expenditure

10. As disclosed in note 52 to the financial statements, the municipality incurred unauthorised expenditure of R3 190 504, as a result of overspending the budget.
11. As disclosed in note 53 to the financial statements, the municipality incurred fruitless and wasteful expenditure of R861 976, as a result of interest charged by suppliers.
12. As disclosed in note 54 to the financial statements, the municipality incurred irregular expenditure of R58 544 464, as it did not follow proper supply chain processes.

Other matters

13. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited disclosure notes

14. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion on it.

Unaudited supplementary schedules

15. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion on them.

Responsibilities of the accounting officer for the financial statements

16. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and Dora, and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
17. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

18. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
19. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

Report on the audit of the annual performance report

Introduction and scope

20. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected key performance areas presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
21. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators/measures included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.

22. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected key performance area presented in the annual performance report of the municipality for the year ended 30 June 2018:

Key performance area	Pages in the annual performance report
Key performance area – basic service delivery	xx – xx

23. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
24. The material findings in respect of the usefulness and the reliability of the selected key performance area are as follows:
- Number of areas/locations serviced with access to solid waste facilities
25. The source information, evidence and method of calculation for achieving the planned indicator were not clearly defined.
26. The planned target for this indicator was not specific in clearly identifying the nature and required level of performance.
27. The systems and processes that enable reliable reporting of achievements against the indicator were not adequately designed, as it did not clearly identify the source and the method of calculation for the indicator.

Number of informal settlements targeted for formalisation

28. The planned target for this indicator was not specific in clearly identifying the nature and required level of performance, and did also not specify the period for delivery.

Other matters

29. I draw attention to the matters below.

Achievement of planned targets

30. Refer to the annual performance report on pages xx to xx for information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on the usefulness of the reported performance information in paragraphs 25 to 28 of this report.

Adjustment of material misstatements

31. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of basic service delivery. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness of the reported performance information. Those that were not corrected are reported above.

Report on the audit of compliance with legislation

Introduction and scope

32. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.
33. The material findings on compliance with specific matters in key legislation are as follows:

Annual financial statements, performance report and annual report

34. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of non-current assets and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.
35. The local community was not invited to submit representations in connection with the 2016-17 annual report, as required by section 127(5)(a) of the MFMA.

Expenditure management

36. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
37. Reasonable steps were not taken to prevent irregular expenditure amounting to R58 544 464, as disclosed in note 54 to the financial statements, as required by section 62(1)(d) of the MFMA. The majority of the disclosed irregular expenditure was caused by not stipulating in the bid documents, the minimum threshold for local production.
38. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R861 976, as disclosed in note 53 to the financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by interest charged on supplier accounts.

39. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R3 190 504, as disclosed in note 52 to the financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by the overspending of the budget.

Asset management

40. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.
41. Capital assets were transferred and disposed of without the municipal council having, in a meeting open to the public, decided on whether the assets were still needed to provide the minimum level of basic municipal services; or having considered the fair market value of the assets and the economic and community value to be received in exchange for the assets, as required by section 14(2)(a) and 14(2)(b) of the MFMA.

Procurement and contract management

42. Bid documentation for the procurement of commodities designated for local content and production did not stipulate the minimum threshold for local production and content, as required by preferential procurement regulation 8(2) of 2017. Similar non-compliance was also reported in the prior year.

Human resource management

43. Appropriate systems and procedures to monitor, measure and evaluate performance of staff were not developed and adopted, as required by section 67(1)(d) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000).

Consequence management

44. Unauthorised expenditure was certified by the council as irrecoverable without first having adopted an investigation report to determine the recoverability of the expenditure, in contravention of section 32(2)(a)(ii) of the MFMA.
45. Irregular expenditure was certified by the council as irrecoverable without first having adopted an investigation report to determine the recoverability of the expenditure, in contravention of section 32(2)(b) of the MFMA.
46. Fruitless and wasteful expenditure was certified by the council as irrecoverable without first having adopted an investigation report to determine the recoverability of the expenditure, in contravention of section 32(2)(b) of the MFMA.

Other information

47. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report, which includes the accounting officer's report and the audit committee's report. The other information does not include the financial statements, the auditor's report and the selected key performance area presented in the annual performance report that has been specifically reported in this auditor's report.
48. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
49. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected key performance area presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
50. I have nothing to report in this regard.

Internal control deficiencies

51. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the annual performance report and the findings on compliance with legislation included in this report.
52. There was inadequate oversight and monitoring of the implementation of internal controls during the year, resulting in material misstatements in the financial statements and annual performance report as well as instances of irregular expenditure.
53. The municipality did not develop and implement proper performance planning and management practices to provide for the development of performance indicators and targets, as some did not meet the 'SMART' criteria as defined in the Framework for Managing Programme Performance Information.

54. Non-compliance with legislation identified in procurement and contract management relating to deviations that were not justifiable and local content requirements that were not stipulated, could have been prevented had compliance been properly reviewed and monitored. In addition, non-compliance due to material misstatements identified in the financial statements submitted for auditing could have been prevented had proper reviews been done by senior management.
55. The supporting documents to the financial statements and annual performance report were not adequately reviewed.

Auditor - General

Mbombela

30 November 2018



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure – Auditor-general's responsibility for the audit

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for the selected key performance area and on the municipality's compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the financial statements as described in this auditor's report, I also:
 - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control
 - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer
 - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor's report. However, future events or conditions may cause a municipality to cease continuing as a going concern
 - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation

Communication with those charged with governance

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.